

State of California

Public Utilities Commission
San Francisco

M E M O R A N D U M

Date : September 21, 2005

**To : The Commission
(Meeting September 22, 2005)**

From : Randy Wu, General Counsel

Subject: General Counsel Wu Report: Additional Addendum to Summary of Material Terms of DWR Financing Documents; to provide for refinancing a portion of DWR's Power Supply Revenue Bonds.

The Department of Water Resources (DWR) is proposing to refinance a portion of its outstanding Power Supply Revenue Bonds in order to lower its overall interest costs. To facilitate this transaction it is asking the CPUC to approve a 2005 Addendum to Summary of Material Terms of Financing Documents. The proposed document is now available for public review. This document will be presented to the Commission for approval as Item #42 on the Commission's September 22 agenda.

Any interested persons wishing to comment on this matter may do so during the Public Comment portion of the Commission's September 22nd meeting, or by submitting written comments by e-mail to General Counsel, Randolph Wu at rwu@cpuc.ca.gov, no later than 6 pm on Wednesday September 21st.

DWR will be sending a memo to the CPUC providing further information about the proposed refinancing. This memo will be posted as soon as it is available.

DEPARTMENT OF WATER RESOURCES

CALIFORNIA ENERGY RESOURCES SCHEDULING

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SACRAMENTO, CA 95821-9001

(916) 574-1291



September 21, 2005

Mr. Randolph L. Wu, Esq.
General Counsel
California Public Utilities Commission
505 Van Ness Avenue
San Francisco, California 94102

Dear Mr. Wu:

Department of Water Resources (DWR) has determined that current market conditions make it likely that debt service savings can be achieved by the issuance of bonds for the purpose of refunding a portion of DWR's outstanding power revenue bonds, thus reducing the debt service cost which must be recovered through Bond Charges for the life of the bonds.

In the proposed transaction, DWR would issue variable rate debt to retire/defease current fixed rate debt. DWR would also enter into interest rate swaps under which DWR would pay a fixed rate and receive a variable rate designed to match the interest rate on the refunding bonds. DWR would also enter into credit and liquidity facilities associated with the variable rate refunding bonds. DWR's existing unhedged variable rate debt, which is about 25 percent of its total outstanding debt would remain in place. In the original 2002 bond issue, DWR issued \$1.4 billion of variable rate debt with interest rate swaps, which are similar in structure to the proposed refunding bonds.

DWR has received Governor's Office approval to proceed with the transaction, and DWR plans to implement the transaction so long as current market conditions continue. The Department of Finance has selected Lamont Financial to help oversee the transaction for the State. They are in addition to the DWR's financial advisory firm, Montague DeRose, and the State Treasurer's participation in the transaction.

Under current market conditions, DWR anticipates that the refunding would achieve at least \$100 million net present value savings to ratepayers over the life of the bonds, resulting in approximately \$8 to \$10 million savings per year.

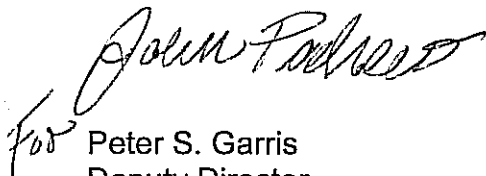
If market conditions continue, DWR plans to enter into the swaps in the last week of September and then issue the variable rate refunding bonds by the end of November.

Mr. Randolph Wu, Esq.
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Under Section 7.10 of the Rate Agreement between DWR and the Commission, in 2002 DWR submitted to the Commission a Summary of Material Terms of the bonds to be issued and an Amended and Restated Addendum to the Summary of Material Terms. In brief, the issuance of the refunding bonds as proposed would be a material change in the amount of bonds described in the Summary and Addendum, resulting in the need for the Commission to authorize its designee to approve such change.

Please contact Jim Olson, Deputy Controller at (916) 574-1297 or me at (916) 574-2733 if there are any questions.

Sincerely,

A handwritten signature in cursive script, appearing to read "Peter S. Garriss".

For Peter S. Garriss
Deputy Director
California Energy Resources Scheduling

Attachment

cc: (See attached list.)

Honorable Michael R. Peevey, President
California Public Utilities Commission
505 Van Ness Avenue
San Francisco, California 94102

Honorable Geoffrey F. Brown, Commissioner
California Public Utilities Commission
505 Van Ness Avenue
San Francisco, California 94102

Honorable Susan P. Kennedy, Commissioner
California Public Utilities Commission
505 Van Ness Avenue
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Honorable Diane M. Grueneich, Commissioner
California Public Utilities Commission
505 Van Ness Avenue
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Honorable John A. Bohn, Commissioner
California Public Utilities Commission
505 Van Ness Avenue
San Francisco, California 94102

Mr. Joel T. Perlstein, Esq.
California Public Utilities Commission
505 Van Ness Avenue
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THIS ADDENDUM TO SUMMARY OF MATERIAL TERMS OF FINANCING DOCUMENTS, dated as of September 20, 2005 (the "2005 Addendum"), is a supplement to the Summary of Material Terms of Financing Documents ("Summary of Material Terms") which was attached to a memorandum dated February 21, 2002 from the California Department of Water Resources ("DWR") to the California Public Utilities Commission ("CPUC") as Attachment A, as the same was supplemented and amended by an Amended and Restated Addendum to Summary of Material Terms dated as of August 8, 2002 (the "Amended and Restated Addendum"). All undefined terms in this 2005 Addendum shall be defined by reference to the Rate Agreement dated as of March 8, 2002 (the "2002 Rate Agreement") between DWR and CPUC and the Trust Indenture dated as of October 1, 2002, among DWR, the Treasurer of the State of California, as Trustee, and U.S. Bank, N.A., as Co-Trustee.

DWR has determined that current market conditions make it likely that debt service savings can be achieved by the issuance of Bonds ("Refunding Bonds") for the purpose of refunding a portion of its outstanding Bonds and by entering into related Financing Documents, Enhancement Facilities and Qualified Swaps, thus reducing the costs which must be recovered through Bond Charges.

The Summary of Material Terms and the Amended and Restated Addendum specified certain matters which were reflected in the terms of the Financing Documents and addressed matters relating to the issuance of Bonds for the purpose of repaying advances from the General Fund and the Interim Loan. This 2005 Addendum addresses matters relating to the proposed issuance of Refunding Bonds by DWR, including specifying that the Refunding Bonds are not subject to the maximum aggregate

principal amount and proceeds limitations reflected in the Summary of Material Terms and the Amended and Restated Addendum and are instead subject to the limitations reflected herein and in the 2002 Rate Agreement.

1. Maximum Amount of Refunding Bonds Authorized.

DWR will issue no more Refunding Bonds than it determines are necessary to provide for the defeasance of the Bonds to be refunded and to pay Costs incurred in connection with the issuance of the Refunding Bonds, the execution and delivery of the related Financing Documents, Enhancement Facilities and Qualified Swaps and the defeasance and redemption of the Bonds being refunded, provided that the maximum aggregate principal amount of Refunding Bonds which may be issued pursuant to this 2005 Addendum will not exceed \$2,700,000,000.

2. Use of Proceeds.

DWR will apply the proceeds of the Refunding Bonds to fund an escrow providing for the defeasance of Bonds being refunded and to the payment of Costs incurred in connection with the issuance of the Refunding Bonds, the execution and delivery of the related Financing Documents, Enhancement Facilities and Qualified Swaps and the defeasance and redemption of the Bonds being refunded. The particular Bonds to be refunded and the principal amount to be refunded will be determined by DWR based upon market conditions and other relevant factors such as rating agency considerations.

3. DWR Determination as to Savings.

Prior to the issuance of the Refunding Bonds, DWR will furnish to the Commission DWR's determination that there are present value savings projected to result from the issuance of the Refunding Bonds and the projected amount thereof, which will not be less than the lesser of \$100,000,000 or 4% of the amount of the bonds being refunded. Such determination will include a summary of the principal assumptions used in making such determination. The Department will, in the course of preparing to issue the Refunding Bonds and make such determination, provide to the Commission such information as the Commission may request concerning matters relating to such determination and the assumptions therein.

4. Rate Agreement Applicable to Refunding Bonds.

The Refunding Bonds shall be entitled to the benefits of the Rate Agreement in accordance with the terms thereof.